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SENSITIVE

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SUBJECT: GERMANY DIVES DEEPER INTO RECESSION

REF: A. BERLIN 1538
[1](#)B. BERLIN 1677

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[1](#)1. (SBU) SUMMARY. After several years of strong growth and falling unemployment, the German economy is on the ropes. The German government has repeatedly revised its 2009 growth forecasts downward, and the Economics Ministry is now projecting that gross domestic product will shrink by 2.25 percent in 2009. Exports) the engine of Germany,s economic growth) are likely to decline by almost 9 percent in 2009. Unemployment will rise to 8.4 percent in 2009, up from 7.8 percent in 2008. Most German economists are greeting the government,s second stimulus package with relief, but recognize that its full impact will not show up until the second half of the year at the earliest. Also, given Germany,s dependence on exports, the recovery will depend heavily on what other major countries do to revive their economies. END SUMMARY.

SHARP CONTRACTION IN 2009

[1](#)2. (U) Germany is facing its biggest economic downturn since World War II. According to the government,s annual economic report released on January 21, the German economy will contract by up to 2.25 percent during 2009) markedly worse than the government,s previous estimate of plus 0.5 percent growth. The report notes that German gross domestic product (GDP) increased by 1.3 percent overall in 2008, following 2.5 percent growth in 2007. &There is no precedent in post-war history for this economic decline that we unfortunately have to forecast,8 commented economics minister Michael Glos at his January 21 press conference. (Germany,s most significant previous contraction was in 1975, when its economy shrank by 0.9 percent in the wake of the oil shock.) He made no firm prediction for Germany,s economic performance in 2010, indicating the government would produce another forecast in April at the earliest. However, Glos said he expected the world economy to be growing again by then.

UNEMPLOYMENT ON THE RISE

13. (U) The recession's other shoe dropped last month when German unemployment increased for the first time since February 2006, thus ending an unprecedented 34-month labor market expansion. Figures released by the Federal Employment Agency on January 8 showed that the number of those seeking employment in Germany rose by 18,000 in December. The change was small, but the significance great, since it likely heralds many more months of rising unemployment. Employment Agency Chief Frank-Juergen Weise warned that unemployment could eventually top 4 million (up from the current 3.1 million.) Minister Glos said he expected unemployment to climb from 7.8 percent in 2008 to 8.4 percent this year.

14. (SBU) Employers are scrambling to cushion the blow. The chief economist of the national employers, federation, BDA, Ottheinrich von Weitzershausen, told Econ/Labor Counselor that many BDA member companies wanted to keep their employees on the payrolls, at least for now. Dismissals would primarily affect temporary workers or those employees working under fixed-term contracts, he said. The federal government's extension of short-time benefits would also help companies to keep staff. Many companies learned their lesson from the 2003 recession, he said; in the context of skilled worker shortage and a shrinking work force, they now try to hold onto their workers as long as possible. However, he saw trouble on the horizon, notably among automobile firms and their suppliers, which have built up huge overcapacities in recent years.

EXPORTS FALL OFF CLIFF

15. (U) An explanation for the jump in unemployment is not

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hard to find. German exports posted a record 10.6 percent fall in November (after declining 0.6 percent from September) as orders for cars and machinery (mainstays of the manufacturing sector) plummeted. This is the biggest monthly drop since records for a reunified Germany began. Overall 2009 exports will likely decline by 9 percent, according to a government report.

16. (U) The news shocked the markets. Unicredit analyst Alexander Koch, for instance, called the figures &horrible.8 The fact that German companies were in good shape and otherwise competitive was irrelevant, he said; the collapse in global demand had been devastating. Koch explained that the slowdown in trade weighed massively on growth in the fourth quarter of 2008. The head of foreign trade at the Federation of German Chambers of Industry and Commerce (DIHK), Axel Nitschke, said the future looked grim, especially given the problems besetting the automobile industry. &December,s trade figures (to be released on February 9) will be even worse,8 he said. Germany,s trade surplus narrowed from 19.4 billion euro in November 2007 to 9.7 billion euro in November 2008; this is close to half the April level of 18.8 billion euro.

MANUFACTURING IN FREEFALL

17. (U) Reflecting the decrease in exports, the German manufacturing sector is also suffering record declines. According to provisional data from the Federal Statistical Office, manufacturing turnover fell by an adjusted 6.4 percent in November 2008 compared with November 2007 (following a revised 3.2 percent drop in October 2008). This was the steepest decline since 1990. Car manufacturers and the chemical industry suffered in particular. Chemical Giant BASF, carmakers Volkswagen AG and BMW are among companies that have suspended production, canceled shifts and shortened working hours in recent weeks. German car sales fell last year to the lowest level since 1990.

ANY RAYS OF HOPE?

¶8. (SBU) Recovery will be slow. Thomas Szewczyk, the Bundesbank's Berlin Representative, told EMIN that the fourth quarter of 2008 and first quarter of 2009 would likely mark the trough of the economic downturn. The Bundesbank saw the possibility of some very modest growth beginning in April. This is partly because of stimulus packages by Germany's trading partners, he said. Though Szewczyk expects the modestly positive growth to continue from April through the end of the year, overall 2009 GDP growth will remain negative due to the depth of the current slump.

¶9. (SBU) The new stimulus plan should help, but most analysts believe its full impact will not be felt any time soon (REF B). According to Ulrich Walwei, Deputy Director of the Employment Agency's Institute for Labor Market and Vocational Research (IAB), the 50 billion euro package approved by Chancellor Merkel's cabinet on January 27 could offset the expected contraction by 0.5 to 1.0 percentage points, thereby saving up to 250,000 jobs. He warned, however, that the plan's impact on employment might not be felt until 2010. Szewczyk likewise confided to EMIN that the Bundesbank would have preferred a front-loaded stimulus initiative that focused more on consumption than on investment.

¶10. (SBU) Some are more upbeat. Anton F. Boerner, President of the Federation of German Wholesale and Foreign Trade (BGA), said the government's forecast for exports may be too pessimistic. BGA is expecting a decline in German exports in the range of 3 to 4 percent this year, Boerner said. In his view, President Obama's stimulus package would help the U.S. economy recover more quickly than most economies in the EU, which in turn would help boost global trade to the benefit of Germany's export-driven economy.

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COMMENT

¶11. (SBU) Many Germans are now seeing the downside of their economy's export dependency. The price of being the "export world champion" is that the German economy's fate hinges primarily on the revival of economic activity in Germany's trading partners. Focusing on investment rather than consumption, Chancellor Merkel's 50 billion euro stimulus plan does little to plug the gaping hole in the Germany economy left by collapsing global demand. With the exception of some Bundesbank officials and enlightened Bundestag members, few German policymakers have an appetite for measures to redress the country's enormous net trade surplus. There is therefore disproportionate interest in the stimulus plans under consideration in Germany's trading partners, including the United States. END COMMENT.
Koenig